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Sessional Committee I

SUSTAINABLE DEVELOPMENT: THE EFFECT OF INTERNALIZATION OF EXTERNAL COSTS ON SUSTAINABLE DEVELOPMENT

Draft agreed conclusions submitted by the Chairman

In accordance with Conclusion 407 (XL) of the first part of the fortieth session of the Trade and Development Board, Sessional Committee I held an exchange of views on the effect of the internalisation of external costs on sustainable development. Its discussion was aided and enriched by the excellent documentation prepared by the UNCTAD secretariat and the contributions of a panel of experts drawn from several regions.

The Committee agreed that:

1. The internalisation of external environmental costs is of general importance in the follow-up to UNCED, particularly in the light of the Rio Principles, especially Principle 16. Internalisation will be an important instrument for achieving sustainable development. Internalisation will also relate to the further evolution of multilateral discussions on trade and environment, in UNCTAD, WTO and elsewhere.

2. Internalisation requires a careful balancing of equity and efficiency and, within the former, of intra- and inter-generational considerations of domestic and international nature. It is a means towards the ultimate goal of the efficient avoidance of environmental costs, not a goal in itself.

3. Internalisation may be accomplished in three basic ways, all of which may be used in combination. The regulatory approach has the advantage of ensuring compliance to strict quantity-related standards, but only if there is adequate enforcement. Market-based economic instruments are often the most cost-efficient and create a continuing incentive to reduce external environmental costs. Such instruments, however, make the true costs of environmental protection highly visible and require the existence of markets and administrative structures which may not be adequately developed in some countries. A third approach consists in undertaking public education and information programmes to alter the public's perception of environmental costs.

4. Success in achieving internalisation within a given country is likely to be improved if attention is paid to the following elements, inter alia, of a potential policy mix:

(a) Attenuation or elimination of policies that distort resource allocation, in particular, environmentally-unsound subsidies. Agricultural subsidies are of importance in this context, particularly those which have a trade effect;

(b) Correction of fundamental incentive failures, such as insecure or absent property rights, or unpriced resources;

(c) Gradual introduction of other internalisation policies of a regulatory or economic nature. These could include product or emission charges, other economic instruments for internalisation and the reinforcement of institutional capacity in the environmental area;

(d) Environmental impact assessment in public decision making, in particular concerning public projects.

5. Sound macroeconomic policies, a strong fiscal system, the development of human resources in environmental management and administrative efficiency are essential for successful internalisation.

6. In addition to measures at the national level, an efficient system of positive incentives at the international level would help to induce cooperative environmental protection with special attention directed towards developing countries, in line with Principle 7 of the Rio Declaration.

7. Trade has an essential role to play as a vehicle for internalisation. The successful implementation of the results of the Uruguay Round, particularly in the areas of market access and subsidies, could contribute towards making internalisation easier to accomplish. However, the contribution of trade liberalisation to sustainable development will be achieved only when the liberalization is accompanied by government policies to ensure the adjustment of economic incentives to environmental objectives. The introduction of certain market-based instruments may also help to spur internalisation, but care needs to be taken in designing and implementing them to avoid undue adverse effects on the exports of developing countries. Moreover, policies to internalise external environmental costs may affect competitiveness.

8. Commodity pricing issues and the coordination of internalisation in commodity-based industries are central to making trade better serve the objectives of sustainable development. Commodity production and processing impose costs on the environment, and ultimately on those living in areas where these activities take place, which are rarely included in the market price. Mechanisms may be needed to deal with such market failures, without thereby diminishing the resources derived, particularly by the developing countries, from commodity exports.

9. External environmental costs frequently arise from the techniques of production rather than from the product. Technologies already available can provide solutions and potential future technologies hold out the prospect of substantial improvements in production techniques. The heavy financial costs associated with the transfer of "clean" technologies will, however, make necessary the adoption of cooperative approaches which include, in particular, the private sector, to provide incentives for switching to more environmentally sound technologies.

10. Work in UNCTAD on the issue of internalisation should now assume more specific directions. It is an important element within the programme on trade and environment outlined in Conclusion 407 (XL). The issue of competitiveness will be considered at the first part of the Board's forty-first session. It would be useful to establish a special institutional mechanism for dealing with the inter-related areas of trade, environment and development. There is general agreement to undertake work in the Standing Committee on Commodities to examine the issue of the principle of full cost resource pricing and its implementation in support of sustainable development. There is also agreement that issues relating to financial aspects of sustainable development as well as to cooperative solutions to the problems associated with the transfer of environmentally sound technologies to developing countries, deserve further consideration in UNCTAD.

The Committee recommended that:

11. The Trade and Development Board request the Standing Committee on Commodities to begin examination at its next session of "global cooperation on the principle of full cost resource pricing and its implementation, in support of sustainable development".